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STATE FOR NEA/ARP (MASILKO)

E.O. 12958: DNG: CO 03/05/2034

TAGS: ECON EFIN AE

SUBJECT: (S) UAE CONSIDERS CENTRAL BANK RESTRUCTURE AND
ENHANCEMENT

REF: 08 ABU DHABI 1381

Classified By: Ambassador Richard Olson, for reasons 1.4 b and d.

THIS IS AN ACTION CABLE

¶1. (S//NF) Summary. On March 2-3, U.S. Treasury Department central banking advisors from the Office of Technical Assistance (OTA) met with UAE Central Bank officials to discuss possible UAEG efforts to restructure and enhance its Central Bank. While the Central Bank officials expressed a clear desire to improve the regulator's ability to respond to financial crises such as the one currently unfolding, they remain divided on the extent and ultimate goals of the reform exercise. Central Bank officials representing Dubai are pressing for a broad initiative that will lay the ground work for an eventual GCC Central Bank located in the UAE. UAE Central Bank officials representing Abu Dhabi have yet to embrace the more far reaching goals of their genetically ambitious neighbor. OTA was represented by central banking advisors Thomas Simpson and Peter Nicholl, and debt advisor Michael Grifferty, joined by Treasury Attach and Econ Chief. They met with UAE Central Bank Chairman Khalil al Foulathi, Governor Sultan bin Nasser al Suwaidi, board members Mubarak al Mansouri and Khalid Balama, and advisors Dr. Nasser Saidi and Ra'ed Saqfelhait. End Summary.

(S//NF) DUBAI PREPARES TO HOUSE GCC CENTRAL BANK

¶2. (S//NF) Dr. Nasser al Saidi, advisor to Dubai-based UAE Central Bank Vice Chairman Dr. Omar bin Sulaiman, laid out a clear path by which the UAE could preempt other GCC nations and succeed in securing the right to permanently host the GCC central bank. Dr. Nasser explained how the UAE is ideally positioned to accommodate the eventual GCC central bank as it has already built the most active financial sector in the Gulf with the presence of most major international financial institutions, newly developed foreign exchange clearing and payments systems, and a welcoming environment suitable for international staff and visitors. According to Dr. Nasser, UAE Central Bank Vice Chairman Dr. Omar believes the current turmoil in the UAE's financial sector has created the right opportunity to drive through a financial sector and regulatory modernization plan that will lay the foundation for the GCC central bank to reside in the UAE. (Note: Dr. Nasser opined in a side bar that the UAEG would likely accept a Saudi national at the head of a GCC central bank, provided that the institution is physically located in the UAE. Dr. Nasser is the former First Vice Governor of the Central Bank of Lebanon. Dr. Omar also serves as the head of the Dubai International Financial Centre. End Note.)

¶3. (S) Dr. Nasser explained that the UAE embarked on a nationwide modernization plan over two years ago that seeks to improve governance in the UAE. The impetus for Central Bank reform has been more recent, with the onset of the financial turmoil exposing significant areas of weakness in the UAE's financial sector and oversight bodies. This

experience is the first major financial crisis for the UAE, affecting its banking, credit and real estate sectors. UAE financial authorities have responded sub-optimally to the crisis as they lack effecting fiscal and monetary policy tools. In fact, Dr. Nasser confirmed that the UAE Central Bank has no tools in place to help the banking sector, and therefore had to invent them on the fly. Additionally, the federal structure of the UAE, combined with and its highly fragmented regulatory and supervisory architecture, has restrained the government from implementing swift and decisive action. As a result, Dr. Omar is leading an effort to reinforce the authority of the Central Bank and widen its scope of supervision as a means to upgrade the UAE's entire financial sector, a core component of the UAE's aggressive economic development plans. In this manner, the UAE Central Bank will drive the reform process of the entire UAE financial and banking sector.

¶4. (S) Dr. Nasser requested the assistance and involvement of the U.S. Treasury Department in several areas. Dr. Nasser and Ra'ed shared that with the approval of the Central Bank board, they are currently reviewing proposals from four international consulting firms. The proposals identify areas for improvement in financial sector regulation and detail implementation roadmaps. They have narrowed the field to two firms and will be selecting their final partner in the coming weeks. Dr. Nasser requested that U.S. Treasury provide feedback on the proposals submitted by the remaining consultants.

¶5. (S) Once a consulting firm is agreed upon, Dr. Nasser welcomes U.S. Treasury involvement on various technical elements, such as IT, operations, payments systems, economic research, statistics, formulation of monetary policy, and strategic planning for the Gulf Monetary Union. He foresees the need for U.S. Treasury assistance in setting up bond and money markets, to include an auction system for government securities and a deposit guarantee mechanism. Dr. Nasser also envisions Treasury guidance on defragmenting the UAE banking and financial sector, to include markets, regulations and authorities. During the implementation phase, Dr. Nasser hopes for a stream of training programs for Emirati Central Bank officials/employees, tapping the resources of the Treasury Department, Federal Reserve and IMF.

¶6. (S) ACTION REQUEST: UAE Central Bank Vice Chairman has requested an options paper from the U.S. Treasury Department laying out various forms of engagement through which the Treasury Department could support the restructuring effort.

(C) ABU DHABI INVITES IMPROVEMENTS, PROCEEDING WITH CAUTION

¶7. (S) Displaying far less ambition for change than Vice Chairman Dr. Omar, Abu Dhabi-based UAE Central Bank Chairman Khalil al Foulathi and Governor Sultan al Suwaidi peppered the OTA advisors with questions about the global financial crisis and the depth of the U.S. economic recession. The Chairman and Governor confirmed that the Central Bank was reviewing options for possible enhancements and regulatory restructuring. They solicited advise on how the UAE Central Bank should respond to the current crisis. They questioned the OTA advisors on various models and functions of financial oversight, including lessons learned from the U.S.'s fragmented structure which holds commonalities with the UAE system. They asked for OTA views and experiences on how to confront inflation within the confines of a fixed exchange rate currency regime.

¶8. (S) In a side bar following the conclusion of the meeting, Governor Suwaidi approached OTA advisor Simpson and requested Treasury's assistance as a second set of eyes to review the final restructuring proposal from the selected consulting firm.

¶9. (S//NF) COMMENT. While tension may exist between Abu Dhabi and Dubai as to the extent of reform needed in the UAE's financial sector and supervisory authorities, the UAE is

clearly embarking on a path of modernization. Moreover, Central Bank Vice Chairman Dr. Omar, who also serves as the head of Dubai's financial free zone, the Dubai International Financial Centre, has a proven track record of delivering financial sector reform. Several high level USG policy initiatives, national security concerns and economic interests are hindered by the fact that the UAE is plagued by an anemic central bank that lacks both authority and capability. The UAE clearly invites U.S. Treasury involvement in its reform effort as a trusted partner in a time of uncertainty, and likely as a source of political cover within the UAE and reputational enhancement internationally. The UAEG relies heavily on international consulting firms to assist in a number of key governmental functions; however, they also understand the limitations of such firms and have been burned by grandiose plans that fail through the execution phase. As such, the UAEG welcomes the experienced and unbiased involvement of U.S. Treasury central banking advisors.

OLSON